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C O N F I D E N T I A L SECTION 01 OF 02 BAKU 000625

SIPDIS

EEB FOR DAN STEIN

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SUBJECT: SOCAR RESTRUCTURING: BACK IN THE USSR

REF: VIENNA 941

Classified By: Charge D'Affaires Donald Lu, Reasons 1.4 (b,d)

11. (C) SUMMARY: In July, President Ilham Aliyev issued and signed several decrees affecting the oil and gas industry, primarily expanding the role and power of the State Oil Company of Azerbaijan (SOCAR). A July 1 decree placed the state gas company, Azerigaz, under SOCAR's control, with the stated goal to "improve the mechanisms of management in the oil and gas industry." A July 20 decree detailed the structure of the state entity defining SOCAR as the country's "economic symbol" abroad. Industry leaders questioned the sagacity of these moves and their implication for future business prospects considering the multiple roles of regulator, partner and competitor SOCAR already plays. End Summary.

12. (C) In a blow to potential western investors' long-held hopes for the privatization of the oil and gas industry in Azerbaijan, President Aliyev issued a decree on July 20 which expanded the mandate and profile of the state oil company SOCAR. These changes were announced after the July 1 decree which brought Azerigaz into the SOCAR fold; effectively creating a linear monopoly from extraction, to production and processing, to delivery. Previously undisclosed administrative details of the state-owned corporation spelled out in the decree were the creation of a board of directors, as well as audit, risk management, procurement, and export departments. Representative offices in London, Geneva, Istanbul and Singapore among others were touted in the announcement. SOCAR's charter capital was also disclosed at 600 million manat (750 million USD).

Keeping Up with the Neighbors

13. (C) Industry observers believe this was a politically-motivated move made to increase SOCAR's brand-image so that it could compete in the international arena with the likes of Gazprom (Russia) and KazMunaiGaz (Kazakhstan). Considering recent developments with the Nabucco IGA (reftel) and other recently publicized discussions among various players in the oil game - Russia, Turkey, Iran - it is conceivable that the GOAJ is looking to add heft to its champion in the hope of increasing its standing in the field.

14. (C) On July 1, the GOAJ subsumed the state-owned gas distribution company Azerigaz to SOCAR under the pretext of "improving" industry efficiency. This came as a bit of a surprise to many in the industry, as Azerigaz had just

received approval from the country's Tariff Council to increase the domestic retail price of gas for private individuals to 100 AZN per thousand cubic meters, in line with the commercial rate which has been in effect since fall 2008. Another surprise was the naming of Alekper Hajiyev, former director of one of Azerbaijan's two oil refineries and relative political unknown, as the new general director of Azerigaz.

They Were a Bunch of Deadbeats

15. (C) In a July 30 meeting SOCAR VP Elshad Nassirov told the Charge that plans for the restructuring had been in the works for quite a while. He noted that now the company has "completed the circle from production to delivery." He also explained some of the reasoning behind SOCAR's absorption of Azerigaz, to include reducing gas theft, eliminating differing rates for industry, creating a real reduction in consumption, increasing oversight, and increasing budgetary inputs. On this last point, he noted that Azerigaz was delinquent in its payments to SOCAR and that now, with SOCAR in control, there would be no excuses. If the end user refused to pay, SOCAR would now have the leverage to simply cut off the gas.

16. (C) Nassirov also pointed out that there would be no privatization of SOCAR production units. He reiterated that production, refining and export would remain state assets, but held that service companies could still be privately owned and operated.

BAKU 00000625 002 OF 002

An Azeri named as BP Azerbaijan President

17. (C) Separately, Embassy has learned from industry contacts on August 5, that Bill Schrader, the Amcit BP Azerbaijan President and head of the Azerbaijan International Oil Company (AIOC) would be replaced as of September 1, 2009 by Rashid Javanshir. Javanshir is a citizen of Azerbaijan, who has worked for BP for 14 years in various leadership roles. In 2006 he became the CEO of the Baku-Tbilisi-Ceyhan (BTC) company and General Manager of the South Caucasus Pipeline (SCP) in charge of onshore operations in Azerbaijan and Georgia, as well as export operations in Turkey. In May 2009 Javanshir was promoted to Executive Vice President of BP Azerbaijan, and President of the company's Shah-Deniz Profit Sharing Agreement (PSA). In addition to his commercial success, Javanshir is an accomplished geological sciences scholar and author of scientific articles and books. Media reports touted the change as the "successful culmination" of the BP Azerbaijan's nationalization plan.

18. (C) COMMENT: Despite SOCAR reports that the consolidation of Azerigaz and branch expansions are aimed at improving the efficiency and overall function of the oil and gas industry in Azerbaijan, industry analysts are doubtful. Many lament that this is a return to the old "Soviet system" of (mis)management.

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